Hershey Foods Corporation
1978 Annual Report

HERSHEY'S Reese's Y&S CANDIES CORY San Giorgio SKINNER Friendly

Mr. Hershey's Home Becomes Corporate Headquarters

Hershey Foods Corporation
Hershey, Pa. 17033
(717) 534-4000

Highpoint, 1913

Soon after the construction of the Hershey chocolate factory began in March 1903, Milton and Catherine Hershey picked the site for the home they had decided to build. A small wooded hill known as "Imboden's Woods" was leased from a neighboring farmer, and surveys were begun in July 1903.

Two years later the tract was purchased, and in the spring of 1906 construction began on a 22-room home which came to be known as Highpoint. Made from native limestone quarried near the site, the building was completed in early 1908.

After Mrs. Hershey's untimely death in 1915, Mr. Hershey divided his time between Highpoint and Cuba. In 1930, the building was made available to the newly organized Hershey Country Club, and Mr. Hershey retained a modest apartment on the second floor. The Country Club used Highpoint as the center of its activities until 1970, when new Hershey Country Club facilities were completed. From 1970 to 1977, Mr. Hershey's home was unoccupied, although Milton Hershey School used it for educational purposes.

In early 1977 Hershey Foods Corporation purchased Highpoint from the Hershey Trust Company, trustee for Milton Hershey School, and began its renovation. Every effort was made to preserve the original design and character of the building. That this has been accomplished is confirmed by the fact that it has been designated a State Historic Site by the Pennsylvania Historical and Museum Commission and been admitted to the National Register of Historic Places, which is maintained by the National Park Service.

Highpoint was occupied by corporate management staff of Hershey Foods Corporation on April 3, 1978. Once again the operation of the Hershey chocolate factory, or more precisely, the company which grew around it, is being directed from the second floor of Highpoint.

The main building houses the offices of the three senior executives, nine corporate officers, and 23 supporting staff members. It also houses a board room, reception areas, several conference rooms, a law library, and various other facilities. The grounds have been landscaped to resemble many of the garden areas which surrounded the facilities when they served as home for the Hersheys.

At the annual meeting of stockholders on April 24, 1978, William E. Dearden, Vice Chairman and Chief Executive Officer, reported in part:

"We have moved the Corporate Headquarters to the renovated home of Mr. Hershey. This move was made because of the great need we have had for additional corporate office space and because we wanted to preserve an important landmark in the history of our company and its founder. This office complex is a first-class facility in every respect and lives up to the image we believe we have as the leader of the Chocolate and Confectionery Industry and one of the leading companies in the Food Industry. If Milton S. Hershey were here today, he would indeed be pleased."

1978 Financial Highlights

(in thousands of dollars except per share figures)

	1978	1977	% Change
Net sales	$767,880	$671,227	+14.4
Income from continuing operations	$ 41,456	$ 36,031	+15.1
Gain on sale of discontinued operation	—	$ 5,300	—
Net income	$ 41,456	$ 41,331	+ .3
Income per common share			
Continuing operations	$ 3.02	$ 2.62	+15.3
Gain on sale of discontinued operation	—	$ .39	—
Net income	$ 3.02	$ 3.01	+ .3
Dividends per common share	$ 1.225	$ 1.14	+ 7.5
Cash dividends paid	$ 16,836	$ 15,251	+10.4
Capital expenditures	$ 37,425	$ 27,535	+35.9
Stockholders' equity	$284,389	$259,668	+ 9.5
Equity per common share at year end	$ 20.69	$ 18.91	+ 9.4
Outstanding common shares at year end	13,745,269	13,730,288	—
Market prices of common stock—range during: First Quarter	19 -21⅝	19½-22⅜	
Second Quarter	21⅛-23½	18¼-20⅞	
Third Quarter	21 -23⅛	17⅞-21⅛	
Fourth Quarter	18½-23¼	16⅝-20	

Quarterly dividends of 30¢ per share for the first three quarters and 32½¢ per share for the fourth quarter were paid on common stock in 1978 compared with 28¢ per share for the first three quarters and 30¢ per share for the fourth quarter for 1977.

Contents

Hershey Foods...

is a major domestic producer of chocolate and confectionery products. Its Chocolate and Confectionery operation has plants in Hershey, Pa.; Oakdale, Calif.; and Smiths Falls, Ontario, Canada. In addition, this operation includes the H. B. Reese Candy Company with its main production facility in Hershey, Pa., and Y & S Candies Inc., a manufacturer of licorice-type candies, with plants in Lancaster, Pa.; Moline, Ill.; Farmington, N. M.; and Montreal, Quebec, Canada.

The Corporation's other principal subsidiaries in 1978 were San Giorgio Macaroni Inc., a regional producer of pasta products, with plants in Lebanon, Pa., Louisville, Ky., and Auburn, N. Y.; and Cory Food Services Inc., Chicago-based provider of one of the nation's largest office coffee service plans.

In early 1979, two other subsidiaries joined the Corporation: Friendly Ice Cream Corporation, which owns and operates over 600 restaurants located primarily in the Northeast and Midwest; and Skinner Macaroni Company, a regional pasta producer located in Omaha, Neb.

Headquartered in Hershey, Pa., the Corporation employed approximately 8,100 people and had 18,735 stockholders on December 31, 1978.

Letter to Stockholders:

Harold S. Mohler

William E. Dearden

Richard A. Zimmerman

It is with pride that we report on the substantial progress being made toward our objective of becoming a major, diversified, international food and food-related company.

Sales and Earnings—The Company achieved record sales of $767,880,000, an increase of 14.4% over 1977, and near record earnings from continuing operations of $41,456,000 or $3.02 per share in 1978, an increase of 15.1% over 1977. Our sales performance reflects market share increases despite intensified competition in the industries in which we operate. Our gains in income were realized in the face of the highest cocoa bean costs incurred in the history of the Company.

Dividend Increase—Importantly, these achievements were not made at the expense of our stockholders or our business. The growth in sales and earnings coupled with the strong financial position of the Company enabled us to increase the cash dividend on the common stock for the fourth consecutive year, and on October 31 the Board of Directors voted to increase the dividend to an annual rate of $1.30 per share. This move is in keeping with our philosophy of providing an appropriate return to our stockholders while also maintaining the Company's fundamental strength through reinvestment of earnings.

Reinvestment in Our Business—The reinvestment in our business is resulting in positive growth. It has been, and continues to be, directed toward research and development for new products and new processes, toward aggressive marketing activity with which to further improve market share, toward improvements in production efficiency and capacity, and toward high quality acquisitions and joint ventures.

Clear evidence of our commitment to research and development is the $7.4 million technical center now under construction in Hershey and scheduled for completion in late 1979. It will enable us to centralize numerous research and engineering functions and expand our efforts in this most important area. The Center also enables us to experiment with sun screening and solar heating panels as new energy sources.

New Products—New products that were introduced in recent years have continued to expand nationally at very acceptable rates. Those introduced in major test markets during 1978 (see pages 6–11) are showing excellent results to date. We have a solid backlog of other new products in various stages of laboratory and consumer testing, and several of these are being introduced on a regional basis in 1979.

Marketing—Significantly, a review of our brand sales during the past 15 years reveals two interesting facts. First, the percentage of our chocolate and confectionery sales attributable to products which are predominantly chocolate (a chocolate content of 70% or higher), has dropped from 84% in 1963 to 59% in 1978. Second, brands introduced or acquired since 1963 account for over one-third of our 1978 chocolate and confectionery sales. We anticipate that this trend will continue in the future.

Record expenditures for selling and marketing our products are planned for 1979. We are again increasing our consumer advertising and trade promotion support for both existing and new brands.

Acquisitions/Joint Ventures—Of special note has been our success in achieving growth and diversification through acquisition. In the pasta area, the addition of Procino-Rossi Corporation, located in central New York State, in April, 1978, and Skinner Macaroni Company, a regional pasta manufacturer in Omaha, Neb. in early 1979 (see pages 16–17), enables us to sell more efficiently and effectively in a larger geographical area which now encompasses most of the United States.

The acquisition of Friendly Ice Cream Corporation, of Wilbraham, Mass., in early 1979 (see pages 18–21), is a major achievement bringing to Hershey a significant leader with an excellent reputation in the "away from home eating" food service industry. This was by far the largest transaction of its kind in Hershey's history. The Company was able to finance $100,000,000 of this acquisition through borrowings under a revolving credit and term loan agreement entered into with four domestic banks. We are currently planning to refinance a substantial portion of this borrowing through the sale of long-term debt securities.

Thus, early 1979 has been a truly extraordinary period for Hershey Foods Corporation. We are especially pleased to report that the management teams and the employees throughout Skinner and Friendly are most enthusiastic about their association with us. We look forward to working with them and to continued growth and development of their businesses.

Also in early 1979, we entered into joint ventures in Brazil with S.A. Industrias Reunidas F. Matarazzo to form two corporations there to manufacture, sell and distribute a variety of food and food related products (see pages 22–23).

Areas of Concern—Inspired and enthusiastic as a result of the successes of 1978 and early 1979, we remain committed to our employees, our communities, and our consumers as we face the challenges of contemporary society. These challenges pose threats and provide opportunities.

The negative impact of domestic inflation combined with the weakening U.S. dollar in the world markets require a unified effort on the part of all Americans. We remain adamant in our belief, however, that government mandated wage/price controls are not the solution.

Such controls have failed in the past, and they are particularly difficult for companies such as Hershey which depend upon foreign commodities, for which controls are seldom imposed or, if imposed, are unworkable. The only solution to this insidious problem which threatens to undermine the competitive enterprise system which has made our country the greatest in the world, is the control of expenditures at all levels of government to the point where they do not exceed the revenues—a balanced budget. This coupled with improved productivity commensurate with wage increases will bring a viability into our economy which is an absolute necessity if we are to survive.

Nevertheless, we will continue to support and cooperate with the President's voluntary program, as evidenced by our prompt response in providing substantiation to the Council on Wage and Price Stability that our November, 1978, price increase was in compliance with the President's guidelines.

Nutrition—In this age of consumer activism, we are concerned with the confusion and uncertainty on the part of consumers regarding the nutritional value of our products. All too often, this has been caused by the misrepresentation of facts and the overreaction by certain constituencies based on emotion and individual value systems as opposed to scientific research that can stand the test of public scrutiny.

We remain the leader in the chocolate and confectionery industry in voluntarily providing nutritional information on the labels of most of our products, having done so since 1974. In this regard, we announced in December, 1978, our intention to voluntarily offer even more product information. Accordingly, the amount of all sugars in our products, both naturally occurring and added, will be included on our labels. We believe this action provides further evidence that we are confident of the quality, safety, and nutritional value of our products, and that we are interested in providing the facts to our consumers.

Consumer Advertising—Even though our advertising strategies are increasingly directed toward adults, we shall continue to oppose any attempt to limit our freedom to advertise to any of our audiences, including children. Children are receiving less than one-third of all our advertising impressions.

In order to build understanding where we believe consumer misunderstanding is being perpetuated, a major program is being launched in 1979 to more effectively disseminate factual information to the consumer about the nutritional value and safety of our products. In this way we are responding to the concerns of the American public while demonstrating our confidence in the quality of our products.

Changes in Board—The year 1978 saw four changes in the Corporation's Board of Directors. On October 31, Richard L. Uhrich, Vice President and Secretary, retired after 48 years of service. He had been a member of the Board of Directors since 1962. Mr. Uhrich served with signal distinction in every position he held with the Corporation since joining it as a clerk in 1930. Another board member, Julian Hemphill, retired after 30 years with the Company and 17 years on the Board.

Francine I. Neff, 35th Treasurer of the United States and a Vice President of the Rio Grande Valley Bank, of Albuquerque, N.M., was elected to the Board in April. Mrs. Neff thus became the first woman to serve on the Board. Richard T. Baker, managing partner of Ernst & Ernst, certified public accountants, until his retirement in 1977, was elected to the Board in July. Mr. Baker resides in Shaker Heights, Ohio.

Executive Changes—Several executive promotions and appointments were announced in 1978. **Dr. Ogden C. Johnson** was named Vice President of Science and Technology to head the newly combined organization of scientific affairs and engineering. He has been with Hershey since 1974. **William Lehr Jr.** was elected Secretary of the Corporation in October to succeed Mr. Uhrich. Mr. Lehr has been with Hershey since 1967. **John S. Harkins**, Vice President, Finance and Commodities, assumed the additional responsibility for the commodities procurement function, which was formerly held by Mr. Uhrich. **Michael F. Pasquale** was appointed to the position of Corporate Controller. He joined Hershey after nine years with Arthur Andersen & Co. **James K. Morris**, who was President of Hershey Chocolate of Canada, was named Chairman, and **David B. Conn** was named President and Chief Executive Officer of that operation.

As in years past, we wish to emphasize the important role our employees at all levels play in the success of the Corporation. Their dedication, industriousness, and loyalty are among its most valuable assets. We offer to them our genuine appreciation for their performance in 1978, and we sincerely believe their continued allegiance and productivity will help to make Hershey Foods Corporation even better tomorrow, thus providing yet greater opportunity for their personal growth and development.

H. S. Mohler
Chairman of the Board

Vice Chairman of the Board
and Chief Executive Officer

R. A. Zimmerman
President and Chief Operating Officer

Board of Directors

Philip A. Singleton,
Harold S. Mohler,
and John C. Jamison

Richard A. Zimmerman
and William E. Dearden

Louis C. Smith,
Francine I. Neff,
and Samuel A. Schreckengaust, Jr.

(*Left*)
John C. Suerth
and Richard T. Baker

(*Right*)
Richard L. Uhrich, who retired on October 31, 1978, after 48 years of service with the Corporation, including 16 years as a member of the Board

(*Above*) Major bar lines (*Below*) Baking products

Chocolate and Confectionery

Hershey Chocolate Company (U.S.A.)

In addition to posting sizeable increases in sales and operating profit under adverse cost conditions, Hershey Chocolate Company (formerly the Chocolate and Confectionery Division) registered impressive market share gains in both its confectionery and grocery product lines and laid the foundation for future growth in all key areas of its strategic plan.

Dollar sales of the chocolate and confectionery industry in the U.S. continued to increase at a moderate rate although tonnage declines are also expected to continue. Hershey products significantly outpaced the industry in both dollar sales and tonnage through a balanced program of high quality products, good value at cost-justified prices, well-known aggressively promoted brand names and wide-spread retail availability.

Multi-million dollar sales increases were enjoyed by all major Hershey brands. Following a successful test market in late 1977 and early 1978, national advertising support was put behind Hershey's Kisses during the Fall of 1978. The expected sales and profit increases were not only achieved but exceeded. Rolo, following start-up of the U.S. production line in late 1977, was expanded to national distribution by mid-1978. Reese's Peanut Butter Cups and Kit Kat continue to be two of the fastest growing major brands in the country. Established brands such as Milk Chocolate with Almond bars, Mr. Goodbar and Miniatures also had important sales gains.

The performance of grocery products was also strong. Hershey's Cocoa responded to a new advertising and publicity program to achieve record sales levels. The line of Hershey's Chips was reformulated and reintroduced with an "All Natural, Real Chocolate" campaign. Sales of this line exceeded 1977 by approximately 59%.

In addition, Reese's Peanut Butter Chips, introduced in the fall of 1977 have become an important factor in the marketplace as well as in the Company's own sales growth. Hershey's Syrup also achieved record sales levels despite heavily-financed competitive programs. Consumer loyalty to Hershey's grocery products is particularly reassuring in light of inflationary pressures and their role as discretionary ingredients.

Significant successes were also registered in the new products program. Reese's Crunchy, test marketed last year, increased its regional distribution in 1978 and will be available nationally in the first quarter of 1979. After Eight, test marketed in 1977 under the licensing agreement with Rowntree Mackintosh Limited, of England, achieved sales and market share targets and has been expanded to a quarter of the U.S.

Two products introduced in 1978 were the result of research and development efforts during 1976–1978. Reese's Pieces, a candy-coated peanut butter flavored item, was introduced in October. This non-chocolate product is a unique and exciting entry in a very large segment of the confectionery market, and initial results are very encouraging. Whatchamacallit, a unique combination of peanut flavored crisped rice center and chocolate coating, was also introduced in October, and the initial response to the product is also most gratifying.

An active program in Research and Development and Marketing Research has identified and developed an inventory of new products that will serve as a foundation for future success in this important area.

Effort has also been beneficially expended in diversifying existing product lines into new outlets. Golden Almond, consolidating its 1977 introductory success, has been joined by a half-pound Hershey's Kiss and three boxed chocolate items imported from the Company's Swedish affiliate, AB Marabou, to form an attractive line of quality gift-boxed chocolates. Realignments in the selling organization have concentrated greater attention on these products, on food service and "fund raising" customers, and on the Alaskan, Puerto Rican and military markets.

Chocolate and Confectionery

	1978		1977
Sales (in millions)	$678.7		$586.9
% Change		+15.6	
Operating profit (in millions) . . .	$ 79.1		$ 69.8
% Change		+13.3	

The figures above relate to continuing operations only.

(*Above*) Beverage mixes, toppings

(*Below*) New market development products

Packaged chocolate and confections

The cost of cocoa beans, the major raw material of Hershey Chocolate Company, continued to increase in 1978. This is the third consecutive year that significant increases in the cost of cocoa beans had to be absorbed into the product line. In addition to the uncertainties normally associated with the highly volatile cocoa market, the weakening of the U.S. dollar inflated the cost of cocoa beans to domestic users.

Sugar, another significant raw material, continued to receive government support to protect domestic producers, and this resulted in higher sugar costs in 1978 despite a lower world market price.

Government supported prices for milk and peanuts increased in line with general price levels in the economy.

Due to a very poor California crop, the price of almonds doubled in cost near the end of 1978.

In November, 1978, the Company announced that continued inflationary pressures necessitated a broad range of price and weight increases, including one that has resulted in the normal retail price of the standard Hershey bar rising from 20¢ to 25¢. These price increases, which received intensive media coverage and governmental scrutiny in response to questions raised at a Presidential news conference, were determined by the President's Council on Wage and Price Stability to be well within the voluntary price guidelines. Trade acceptance of the new prices has been excellent, and the Company is optimistic about the consumer's willingness to pay a fair price of 25¢ for high-quality, popular chocolate.

Y & S Candies Inc., one of the oldest and largest manufacturers and distributors of licorice-type candies in North America, was acquired November 1977. In 1978, a great deal of careful analysis and cooperative effort by both management teams went into planning for the merger of the organizations, operations, and product lines of Y & S and Hershey Chocolate Company into one unit. By combining the distribution, sales and marketing strengths of Hershey with the quality products and management expertise of Y & S, the groundwork was laid for future sales and profitable growth of this non-chocolate confectionery line.

(*Above*) New product development

(*Below*) Hershey Chocolate of Canada products

Production capacity at the Reese plant in Hershey and the Y & S plant in Lancaster was further expanded in 1978. An additional Kit Kat production line, an enlarged finished goods storage area, and new shipping facilities were put into operation at Reese. New processing and packaging equipment was added in a major capital project designed to further expand the newest of the Y & S plants.

Hershey Chocolate of Canada

This company attained record sales in 1978, paced by a strong recovery in the confectionery market. Consumer resistance to higher prices reduced tonnage sales for the grocery products. Despite the increase in sales, the Canadian operation incurred an operating loss for 1978, primarily because gross margin was below plan. In addition, the weakening of the Canadian dollar had an adverse effect.

In May, sales and distribution of Hershey's chocolate and confectionery items and Y & S items were integrated in the British Columbia test market, and sales increased significantly over the previous year. This integration is now being broadened to all other markets throughout Canada.

As in the United States, cocoa bean and almond costs were considerably higher in 1978 than in 1977; and, similarly, the weakening Canadian dollar further accentuated costs of foreign commodities. Milk and sugar prices, meanwhile, rose in line with general price levels of the economy.

Four products were introduced to the Canadian market in 1978. Two taffy-type items—Butterscotch Chew and Chocolate Chew—were introduced nationally in May and October respectively. Reese's Peanut Butter Chips were introduced in the Alberta market in May and expanded to national distribution in September, and Hershey's Kisses were introduced nationally in October. Two new grocery products and two new confectionery products are in various stages of pre-test market development.

On August 21, James K. Morris became Chairman of this operation and David B. Conn was named President and Chief Executive Officer. With the new senior management alignment and the early success with the sales and distribution integration of Y & S with chocolate and confectionery products, we are optimistic about the future of Hershey Chocolate of Canada.


San Giorgio
THIN SPAGHETTI-9
Fettuccini
SHELL MACARONI
LASAGNE
MANICOTTI
Macaroni
ELBOW MACARONI
Delmonico
Alphabets
enriched macaroni
PERCIATELLI-6
P&R
ROSA MARINA-30
SOUPETTES
Orzo-43
PASTINA
Elbow Macaroni
JUMBO SHELLS
RIGATONI
ACINE DI PEPE-27
Light 'n Fluffy
egg noodles
Extra Wide Noodles
rotini
Cut Ziti
enriched
ready-cut macaroni
SPAGHETTI-8
VERMICELLI-10
LINGUINE
LINGUINE-19
THINNER STYLE
Thin Spaghetti
spaghettini
thin spaghetti
spaghetti sauce
SMALL SHELLS-38

Other Food Products and Services

San Giorgio Macaroni

The San Giorgio brand enjoyed large dollar volume increases in 1978, and this subsidiary's growth in market share was among the highest in the pasta industry. During the second year of the Company's introductory program into the New York metropolitan area, progress continued ahead of plan. San Giorgio thereby contributed significantly to an industry-wide growth of 2.4% in tonnage sales following a two-year "no growth" situation in the pasta industry.

Two new products realized very encouraging sales in 1978. The early test market success of Light 'n Fluffy Egg Noodles prompted an accelerated rollout to most major markets, and acceptance there is running ahead of plan. San Giorgio's new "Natural" Spaghetti Sauce was expanded from its initial 1977 test market into a second test market in 1978.

The price of San Giorgio's major ingredient, durum wheat, increased by 17% in 1978 over 1977. The 1979 supply of this commodity, which is a specialty wheat grown only for pasta products, appears to be adequate, and the market price is expected to be stable.

In April, San Giorgio acquired Procino-Rossi Corporation, of Auburn, New York. The P & R brand, which is distributed in New York State markets, particularly the Syracuse and Albany areas, joined the San Giorgio and Delmonico brands. Procino-Rossi adds a strong brand in an important marketing area for San Giorgio.

San Giorgio's modern and efficient plants, its high quality products, and its expanding market strength combined with an anticipated continuation of growth in the pasta industry portend even more impressive results in the future.

Other Food Products and Services

	1978		1977
Sales (in millions)	$ 89.2		$ 84.3
% Change		+5.8	
Operating profit (in millions) . . .	$ 5.1		$ 4.5
% Change		+13.3	

(*Left*)
A selection of San Giorgio Division products


CORY
CORY


CORY
CORY
CORY


CORY


HERSHEY'S
HOT COCOA MIX
HERSHEY'S
HOT COCOA MIX
Cory
non-dairy
COFFEE
CREAMER

Cory Food Services

Cory's major business continued to be its office coffee service program, under which the company provides and services its own brewing equipment in locations to which it sells and delivers coffee and other related products.

Operating profit for Cory Food Services in 1978 was up substantially, as the company experienced a resumption of account growth and a decline in coffee prices. Gross sales were off slightly owing to Cory's withdrawal from the consumer products market and to a reduction in selling price of its office coffee service kits, as decreasing coffee costs were partially passed on to Cory's customers. Because of continued disappointment in the profitability of its brewing equipment and other appliance business, and in order to concentrate more fully on the coffee service business, Cory decided in late 1978 to dispose of its manufacturing operations.

Major accomplishments in 1978 included the introduction of three new Cory-label coffee blends. In addition to offering its customers a choice in product characteristics and price, the Cory-label coffees increased the company's ability to benefit from available quantity discounts, with an attendant increase in gross margins.

1978 also marked Cory's introduction of the Term Discount Plan, a pricing plan which rewards account longevity and volume purchases. The Term Discount Plan and other programs are credited with having produced a significant reduction in customer attrition, which is characteristically high in service industries.

The projected continuation of the trends, activities and programs which produced 1978's operating results also provide optimism for continued growth in the future.

(*left*)
Cory service includes (*clockwise from left*) free use of attractive, professional brewing equipment; Cory's own custom coffee blends, offering a choice in product characteristics and price; computer-cued delivery and service; complete office beverage needs in one convenient service kit; service and repair by people who care.

SKINNER

(*Left*)
Skinner Macaroni Company's modern headquarters and plant facility in Omaha, Neb.

(*Below*)
A selection of Skinner's products

Meet Skinner Macaroni Company

On January 3, 1979, Skinner Macaroni Company, of Omaha, Nebraska, became the fourth pasta company to join Hershey Foods Corporation. Founded in Omaha in 1911, Skinner is the sixth largest U.S. pasta producer, marketing its products in over 20 states. Its plant, built in 1961, is one of the most modern and efficient pasta operations in the U.S. Sales for the year ended June 30, 1978 were nearly $20 million.

Skinner products are sold throughout the Southwest, Southeast, Midwest and some western states. It is the leading brand of pasta products in such markets as Dallas-Fort Worth, Houston, Little Rock, Oklahoma and Omaha. Skinner sells half the macaroni consumed in Texas, Oklahoma, Arkansas and northern Louisiana. It has distribution centers in Arlington, Tex.; Charlotte, N.C. and Birmingham, Ala.

The company was founded by brothers Paul F. and Lloyd M. Skinner. It remained a family-owned enterprise until the merger with Hershey Foods.

Lloyd E. Skinner, son of Lloyd M., has been Chief Executive Officer since 1950. In recent years he has been Chairman of the Board and Chief Executive Officer. W. A. Henry has been President and Chief Operating Officer since 1974, having joined Skinner in 1970 as Vice President/Marketing and Assistant to the President.

Skinner was involved in the cereal business until 1963, when it disposed of those operations and concentrated on operating exclusively in the pasta business. This decision led to the acquisition of Gold Medal Macaroni in 1965, and the Roma Macaroni Co. in 1968. Major Gold Medal distribution is in some southeastern states. Roma's primary distribution is in California and Nevada.

In December, 1961, Skinner moved to its new, fully-automated plant in a suburban industrial tract near Omaha. A one-million-dollar expansion program in 1975 added plant and office space and increased plant capacity from 48-million to more than 65-million pounds annually. In 1977 a microwave production line, costing $1 million, was installed, increasing capacity to 80-million pounds.

Hershey is pleased to welcome the very able personnel of the Skinner organization to its family.

(*Above*)
Magazine advertising

(*Below*)
Vertical ribbon marketing technique

Friendly®

(*Left*) Friendly Ice Cream Corporation headquarters in Wilbraham, Mass.

(*Below*) A selection of foods from a Friendly restaurant menu

Meet Friendly Ice Cream Corporation

During January of 1979, Friendly Ice Cream Corporation was acquired by Hershey in a move that senior executives of both companies hailed as a joining of two dynamic organizations with similar philosophies. This acquisition provides Hershey with a major entry in the food service industry.

Friendly operates a chain of restaurants which serve high quality, moderately-priced menu items and generally specializes in ice cream, sandwiches and informal meals. From its beginnings in Springfield, Mass., in 1935, Friendly has expanded to over 600 units located throughout the Northeast and in much of the Midwest.

The Company is vertically integrated. Most of the food and supplies sold or used in the restaurants are shipped from Friendly's two processing and distribution facilities in its own fleet of refrigerated trucks. Friendly also maintains its own real estate, engineering, construction, carpentry, decorating and maintenance departments. It does not franchise. There are approximately 2,700 full-time and 15,000 part-time employees.

Sales for its fiscal year ended April 28, 1978 were $200,145,000, an increase of 15.2% over fiscal 1977. Net income in fiscal 1978 was $8,845,000 versus $8,723,000 in fiscal 1977.

Friendly's primary marketing objective for the immediate future is to position itself as owner and operator of "informal restaurants," providing full service with a relaxed, informal atmosphere and reasonable prices.

In June, 1935, S. Prestley Blake, 20, had completed his first year of college, while brother Curtis L. Blake, 18, had just graduated from high school. Both wanted summer jobs, but in the depression year of 1935 there weren't many jobs around Springfield, Mass. They settled on the idea of a small neighborhood ice cream shop as a way to earn money.

With $547 borrowed from their parents, the brothers purchased a new 2½ gallon ice cream freezer, an ice cream cabinet, 8 chairs, 2 tables, $16 worth of linoleum and some other equipment. Since they were underage, their mother signed the purchase contract for them. They then rented a store for $35 a month at 161 Boston Road in Springfield.

That modest shop opened on July 18, 1935. After four days of operation, the Blakes switched from ice cream in small cups shaped like cones to double dip ice cream cones—and business boomed. The double dip cone, made with two heaping scoops of ice cream weighing 4-4½ ounces, sold for five cents.

Curt came up with the name "Friendly" for the venture. It represented what the brothers wanted the shop to be—friendly, with good food at a low cost and friendly service.

When the cold weather approached, another menu item was needed to keep customers coming back during the slack ice cream season. A poll taken of regular customers resolved the matter. Customers suggested that hamburgers be added to the menu.

After three years of operation, their landlord proposed that he build the Blakes a new shop right next door. That was the first Friendly expansion.

In 1940, the second Friendly shop opened in West Springfield. It was the first site actually bought by the Blakes for a Friendly store. During 1940, the Friendly Ice Cream company made 23,000 gallons of ice cream and sold $8,000 worth of ice cream cones.

All went well with the two shops until World War II broke out. The brothers kept the two shops open until early 1943, but Curt was soon in the service and Pres in war-related work, so both shops were temporarily closed. Signs were placed in the shop windows confidently stating "This store will be closed until we win the war! This store is not for rent."

In 1945 and 1946 the two shops were re-opened. A third shop was then opened in Longmeadow, Mass. and a fourth in Thompsonville, Conn. The following year, two more shops were added and the Blakes decided to incorporate their growing company. By 1951, Friendly had 10 shops in Western Massachusetts and Connecticut.

Many of the people who presently manage the company came on board during this period. One of these people joined Friendly on a part-time basis in 1946 while pursuing his education. He first worked as a dishwasher, earning 40-cents an hour. He is Robert Gaudrault, now the Chairman and Chief Executive Officer of Friendly.

Ice cream for take-home market

Table-top marketing technique

Friendly Founders Curtis L. and S. Prestley Blake

The third Friendly shop, in Longmeadow, Mass., opened in 1946 and still operating today

Early delivery trucks

Family Restaurant

Throughout the 50's the chain expanded slowly but steadily so that by 1960, there were 50 shops. The chain then doubled in the next five years. Since then, there have been new shop openings in New Jersey and New Hampshire (1965); Rhode Island and New York (1966); Maine (1970); Maryland (1971); Vermont, Pennsylvania, Ohio, Delaware, and Virginia (1972); Michigan and Indiana (1975); and Illinois (1976).

In 1951, the first Friendly Ice Cream plant was built adjacent to the West Springfield Shop with a continuous freezer capable of producing more ice cream. Throughout the expansion of the 50's, this plant provided all the staples of the Friendly menu. But a growing chain of shops combined with optimistic expansion plans for the future persuaded the Blakes to construct a new plant-office complex to handle the ever-increasing work load.

It was completed in 1960 in Wilbraham, Mass. and has since grown to a complex of over 200,000 square feet of building space on a 30-acre tract of land.

The demands of Friendly's midwest expansion resulted in the 1973 groundbreaking for a new $4.5 million food processing and distribution facility, which opened in July, 1975, in Troy, Ohio.

Shops by State Operational Units as of January 26,1979

	Traditional Friendly Ice Cream and Sandwich Shops	Modified Friendly Ice Cream and Sandwich Shops	Friendly Family Restaurants	Friendly Fast Serve Restaurants	SPECIAL'S Fast Food Restaurants	Jim Dandy Stores	TOTAL
Massachusetts	155	13	3	2	1	8	182
New York	37	79	1				117
Ohio	57	9	10				76
Connecticut	61	10	1	1		2	75
New Jersey	3	45					48
Pennsylvania	33		3	1			37
Maryland	22						22
New Hampshire	8	1	2				11
Michigan	8	1	6				15
Rhode Island	5						5
Indiana	4						4
Maine	5						5
Virginia	5		1				6
Illinois	4						4
Delaware	3						3
Vermont	1		2				3
	411	158	29	4	1	10	613

A directory of Friendly restaurant locations was mailed to all stockholders in late February with the 1978 preliminary report.

(*Right*)
The Fudge Cake Sundae, a recent bi-monthly special

International Activities

Nacional de Dulces

AB Marabou

In 1978, Hershey's investment and development activities in the international field expanded considerably. For many years, Hershey Foods concentrated its investments and activities mainly in North America. In today's world, however, the interdependence of markets, currencies, and economies make it unwise for a major industrial company to isolate itself in its domestic market. Also, it is increasingly apparent that certain political, economic, and social events occurring in one part of the globe may have impact and consequence in the U.S. economy.

The policy of forming close associations and ventures with partners abroad who have strong, well-established businesses, and who are willing to keep their own capital at risk in a joint venture situation, seems to respond uniquely and flexibly to this challenge. By the same token, Hershey's reputation for integrity, as well as a sensitivity and appreciation for the ideas and interests of our friends in other parts of the world, also augurs well for successful establishment of such alliances and joint ventures. This pattern of development has worked quite well to date, and along with other forms of diversification, appears to hold good promise for further extension of Hershey's business activities abroad.

To accelerate international business development, the Corporation decided in 1977 to staff an International Department and actively pursue a number of joint venture, licensing, and export opportunities abroad. This organizational structure and centralization of responsibility for international operations brings Hershey's many activities under closer management control, and allows much greater geographical coverage in identifying marketing, licensing, and investment opportunities.

One of the Corporation's most significant development objectives concerns the long-range viability of the cocoa market, which will result in quality cocoa beans, chocolate liquor, cocoa powder and cocoa butter at reasonable prices. In this regard, technical assistance and quality assurance inputs have been provided to suppliers in the Western Hemisphere to improve the quality and yield of chocolate liquor. In connection with this objective, Hershey also has a 22½% interest in Chadler Industrial da Bahia S.A. in Brazil, and respectable earnings levels are being achieved.

In similar vein, Hershey has purchased Hummingbird Hershey Ltd., a cocoa farm located in the Cayo District of Belize, formerly British Honduras. The purpose of this venture is to demonstrate the feasibility of commercial cocoa production and to encourage farmers in the Western Hemisphere to become cocoa growers.

In the Philippines, Hershey has concluded a product licensing agreement and has pledged to the licensee use of its trademark, know-how, and technical assistance in the growth, production, and processing of cocoa beans and in the production and quality control of derived products. The terms and conditions of this trademark, know-how, and technical assistance licensing agreement are currently under review by the Philippines Board of Investment and Department of Agriculture and are subject to their approval. Additionally, in the field of product licensing and technological exchange, Hershey currently has a variety of projects under study in different parts of the world.

A significant step to diversify the Company's growth—in terms of product range and geography—was taken in Brazil with a joint venture in the pasta, biscuit, and margarine fields with the Matarazzo Group. Brazil—with a land mass larger than the United States and half the population of South America—offers tremendous growth potential as a mass market for consumer products.

Matarazzo is one of Brazil's major independent trading companies with operations in chemicals, mining, construction, textiles, paper, agriculture, and food products. Food Division sales in 1977—prior to Hershey's participation—were about $75 million.

Hershey and Matarazzo have formed two joint venture corporations—one a manufacturing company, and the other a sales and distribution company. Hershey owns 40% of each company's capital stock. The manufacturing company was formed with the contribution by Matarazzo of all the assets necessary to manufacture pasta, biscuits, and margarine products. The sales and distribution company has been formed for the purpose of marketing these products, as well as edible oils, flour, candles and soaps.

A new plant site recently started up operations for pasta production in Sao Jose dos Campos, about 100 kilometers north of Sao Paulo. Long-range plans foresee moving the biscuit and margarine plants to this new location.

In 1977, Hershey Foods acquired a 20% interest in AB Marabou of Sweden. Marabou is the leading chocolate and confectionery manufacturer in Sweden and manufactures and distributes a complete line of chocolate and confectionery products, including moulded, enrobed, and boxed chocolates, as well as some starch moulded sugar confectionery items. This company has an important joint venture in the snack food field and, just recently, announced that it has signed a preliminary agreement to purchase the shares of Göteborgs Kex, one of Sweden's leading cookie and cracker producers.

Aside from the direct investment aspects of Hershey's equity participation in Marabou, the Corporation has entered into a joint research partnership and has agreed to exchange certain production technology and know-how to the mutual benefit of both companies. Furthermore, the Hershey Chocolate Company has begun to import several fine quality boxed chocolates from the Marabou range for distribution and sale in the United States.

In Mexico, Hershey's 50/50 joint venture with Anderson, Clayton & Co., S.A.—Nacional de Dulces—continues to develop extremely well, and the company has steadily improved its overall market share. Hershey is greatly encouraged with the success of this operation, as well as the long-term potential offered by the Mexican market, and is actively looking for ways to expand business there.

Another area of concentration for international business development is export sales. In this connection, Hershey's export sales activities have been restructured bringing responsibility for such operations directly under the aegis of the Corporate International group. This change enables the Corporation to put greater emphasis on the export sales of finished products and bulk items currently manufactured by its various domestic product divisions, and work more closely with affiliated companies in expanding exports throughout the world.

S.A. Industrias Reunidas F. Matarazzo

Chadler Industrial da Bahia S.A.

Research and Development

Hershey Foods' new technical center
. . . an architect's model

. . . under construction

Two significant events occurred in 1978 which will help bring the research and development function into sharper focus and give the Corporation one of the best R & D capabilities in the chocolate and confectionery industry.

First, construction of a new 114,000 square foot technical center in Hershey was begun in late April. The facility will enable the Corporation to centralize numerous research and engineering operations, and will contain offices, laboratories, a library, an auditorium, animal testing facilities and a pilot plant. Some of the center's special building features include sun screening and solar heating panels as energy conservation measures. Occupancy of the $7.4 million complex is scheduled for September 1979.

A reorganization of the Corporation's technological and scientific functions into one unit took place in August 1978. Dr. Ogden C. Johnson, former Vice President of Scientific Affairs, was named Vice President of Science and Technology. The new organization will operate as one department in the technical center and consist of four segments: Research, Product and Process Development, Engineering, and Equipment Design and Development.

The Research Group is responsible for developing new knowledge to keep the Corporation competitive in its current business and provide for future growth. Research has concentrated on vegetable fat chemistry, chocolate flavor research, and raw materials such as peanuts and almonds. The Analytical Research Group has gained an international reputation for its chocolate analysis accomplishments. It has developed one of the largest data banks in the world on the nutritional properties of chocolate and cocoa.

Microbiological Research deals with problems relative to Hershey's interests and is particularly strong in the area of cocoa bean microbiology. With the move to purchase more chocolate liquor and less raw cocoa beans from producing countries, this group plays a vital role in insuring that the materials received meet quality specifications. The Nutrition Group concentrates on basic nutrition research projects to enable the Corporation to better understand the nutritional properties of its products. Close contact is maintained with the Chocolate Manufacturers Association Technical Committee, which carries out research on subjects such as tooth decay, acne, chocolate allergy and nutrition.

The Product and Process Development Group is charged with the responsibility of integrating the needs, capabilities and goals of consumers, corporate management, divisional marketing and product development. Long range product opportunities are identified through continuous monitoring of consumer trends and behavioral patterns. For example, the emerging consumer demand for "lightness" has led to San Giorgio's Light 'n Fluffy Noodles and Hershey's Whatchamacallit.

Product planning translates corporate goals into new product objectives. For example, the strategy to reduce the Corporation's dependence on cocoa beans, has led to the development and introduction of Reese's Peanut Butter Flavored Baking Chips and Reese's Pieces. Longer range development is focusing great attention on other foods, including the snack food market, as Hershey discovers ways of linking confectionery technology to other food technology. The goal is to provide the operating companies with new products on a regular basis.

The Corporate Engineering Group has major responsibility for supporting capital programs. It also provides engineering to assist in moving new products into production. The support of the operating divisions' capital programs is essential for continued growth of each division.

The Equipment Design and Development Group provides special support for producing new products and improving existing manufacturing systems. It designs special equipment not generally available "off the shelf" and integrates various items of purchased equipment into a smoothly operating production line.

The Engineering and Equipment Design and Development Groups are both involved in the planning of production lines, and in equipment selection, start up and appraisal. The Equipment Design and Development Group is specifically responsible for the conception of methods and design of special devices to meet requirements unique to Hershey's products and conditions.

Significant advances in the field of solid state technology have precipitated new and innovative approaches to the control of Hershey's manufacturing processes. With the advent of this spiraling technology has come the potential for more stringent control of critical process parameters. The measurement and control of these process variables are essential to the maintenance of consistent product quality. Storage of

process information provides the historical data required for on-going research and development.

The total science and technology program plays a key role in Hershey's ability to meet consumers' needs and remain competitive through quality products which are produced in the most efficient manner from the most suitable ingredients.

Other Corporate Activities

Energy

An energy bill was passed by the 95th Congress, but, as a result of complicated compromises among competing interests, there is little consensus as to what might actually be achieved. One result, however, is readily apparent. The volume of regulations to flow from this new legislation will keep industry busy for some time. A fundamental concern remains as to allocation priorities in the event of fuel shortages.

The situation will continue to affect Hershey through energy price increases, which have averaged 22 percent annually since 1972. Hershey benefits, however, from its Energy Management Program. Through a 15 to 20 percent energy efficiency improvement in manufacturing operations, the Company realizes annual savings of approximately $1.5 million. Hershey has exceeded the energy improvement targets set for the food industry by the federal government for January 1, 1980.

Hershey maintains its position favoring deregulation and decontrol to permit the marketplace to establish the true cost of energy to all sectors—industrial, transportation, commercial and residential.

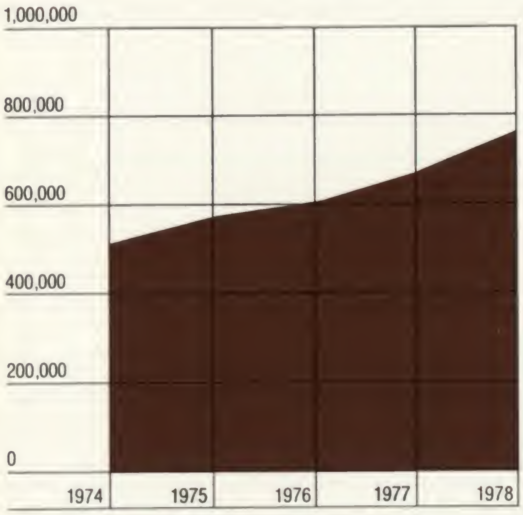
Human Resources

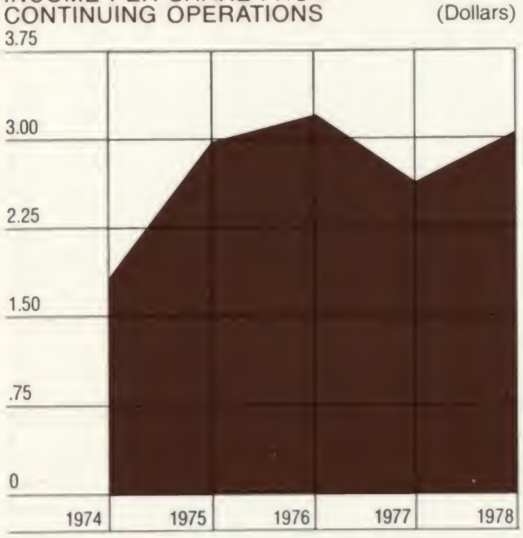
In recognition that sound Human Resources policies contribute significantly to the success and growth of the Corporation, two new programs were initiated in 1978.

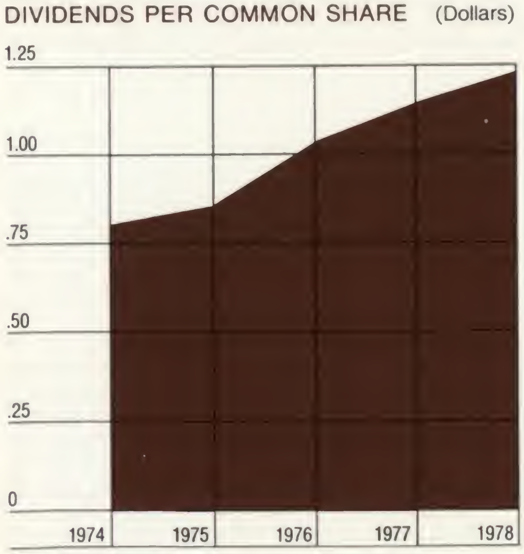
A savings and stock investment plan was designed to facilitate ownership of Hershey Foods common stock by the Corporation's employees. This plan was made available to salaried employees as of July 1, 1978, and has been enthusiastically received.

To foster continued improvement of employee performance, and to assist employees in their own personal development efforts, a performance planning and appraisal workshop has been designed for salaried employees. This program, which focuses on improving manager/subordinate performance discussions, was successfully tested with four separate groups in 1978, and will be extended to others in 1979.

Management's Discussion and Analysis of the Summary of Consolidated Operations







The financial comments relate to the current two year comparative results of operations as well as the five year financial summaries contained on pages 38 and 39.

During the five years ended December 31, 1978, the Company experienced continued growth in consolidated net sales. Net income increased when compared with the prior year for each of the five years presented, with the exception of net income in 1977 which decreased because of a deterioration in gross margins resulting from the unprecedented high level of cocoa bean costs and lower unit volume during this period.

1978 Compared with 1977

Consolidated net sales attained a record level of $767.9 million in 1978. This represents an increase of $96.7 million or 14.4% over 1977 and is the 22nd consecutive year of sales growth. While the Chocolate and Confectionery segment sales increase of 15.6% is attributable to increases in both unit volume and prices, higher prices accounted for the major portion of the sales increase. Sales of the Other Food Products and Services segment increased 5.8% primarily as a result of increases in unit volume. This rate of sales increase was less than the 12.3% increase achieved in the prior year primarily because Cory Food Services, Inc. reduced selling prices as a result of lower green coffee costs.

Raw material costs, principally cocoa beans, continue to remain substantially above the average for recent years. The Company, however, was able to maintain its profit margins in 1978 by price increases implemented in late 1977 and 1978 to offset these higher costs. In addition, in November 1978, the Hershey Chocolate Company increased prices on many items and increased weights and prices on its standard bars. As a result, these bars which sold in most retail outlets for 20¢ now sell for 25¢. The Council on Wage and Price Stability reviewed this price increase and concluded that it was in compliance with President Carter's voluntary anti-inflation program.

Selling, administrative and general expenses increased $17.9 million or 16.3% in 1978 compared with 1977, reflecting an increase of $11.3 million for advertising, promotion and other direct brand expenses as well as the effect of general inflation on other costs during 1978. Also, a provision of approximately $2 million was made for the disposition of the equipment division of Cory.

Shipping expenses increased $4.1 million or 14.2% primarily because of higher shipping rates in 1978.

As a result of the Company's continued strong cash position and rising interest rates, interest income, net of interest expense, was $2.7 million in 1978 compared with $500,000 in 1977.

Net income for 1978 was $41.5 million or $3.02 per share compared with $41.3 million in 1977 or $3.01 per share. Income from continuing operations was $41.5 million or $3.02 per share compared with $36.0 million or $2.62 per share in 1977. This increase in income from continuing operations of 15.1% represents a significant improvement over last year primarily because of increased sales and stable profit margin percentages.

Accounts payable decreased substantially at the end of 1978 compared with 1977 because of large deliveries of cocoa beans at the end of 1977.

1977 Compared with 1976

Consolidated net sales from continuing operations increased by $69.3 million or 11.5% to $671.2 million compared with 1976. The Chocolate and Confectionery segment accounted for $60.1 million of the increase in sales. The increased sales of Other Food Products and Services reflected increased tonnage for pasta and higher selling prices for Cory.

In December 1976, the Hershey Chocolate Company increased prices on many items and increased weights and prices of its standard bars. As a result, these bars, which sold in most retail outlets for 15¢ in 1976, sold for 20¢ in 1977. While dollar sales increased because of higher selling prices, unit volume sales declined for this period.

Costs of cocoa beans, milk, peanuts and almonds were higher in 1977 compared with 1976. Raw material costs for sugar were slightly lower in 1977. To attempt to minimize the effect of the escalating cocoa bean prices during the year, the Hershey Chocolate Company implemented various other price increases and weight reductions on numerous products. Because of the substantial increase in cocoa bean costs for the chocolate and confectionery products, income was

adversely affected since profit margins could not be maintained and this, together with diminished unit sales, resulted in a decline in income from continuing operations.

During 1977, the Company reduced inventory quantities, primarily cocoa beans. This reduction resulted in a liquidation of LIFO inventory quantities carried at lower costs prevailing in prior years as compared with the cost of 1977 purchases, the effect of which decreased cost of goods sold by approximately $8.5 million and increased net income by approximately $4.0 million or $.29 per share. During 1977, cocoa bean prices reached unprecedented, high levels. The Company viewed the economic conditions causing this increase as temporary. Thus, the Company's cocoa bean procurement strategy was to minimize, within operating needs, purchases of this commodity. It is not uncommon for inventory levels to also fluctuate when prices are so volatile.

Selling, administrative and general expenses increased substantially in 1977 compared with 1976 because of increased promotion and selling expenses and higher consumer advertising. Additionally, the general rate of inflation caused an increase in other costs.

As a result of an improved cash position in 1977, the Company had interest income, net of interest expense, of $500,000 compared with interest expense, net of interest income, of $400,000 in 1976.

Income from continuing operations was $36.0 million in 1977 in comparison with $43.7 million in 1976, or a decrease of 17.5%, reflecting a deterioration in gross margins resulting from the unprecedented high level of cocoa bean costs and lower unit volume.

Net income for 1977 reflects the gain on the sale of the real estate and operating equipment of the Company's almond ranch subsidiary, which amounted to $5.3 million after tax or $.39 per share. The assets were sold to Tenneco West, Inc. on June 30, 1977 for $20 million. Since the results of operations of the Company's almond ranch subsidiary were immaterial in 1977, these amounts were included in the results of continuing operations.

Prior Years

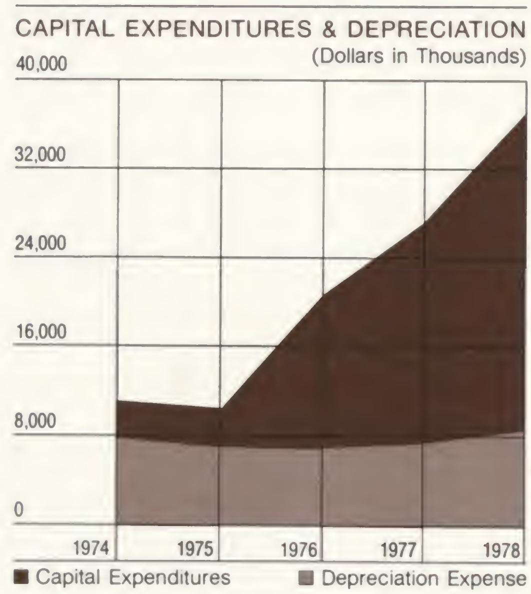
Sales increased in 1976 compared with 1975 primarily because of an increase in consumer units sold. The Hershey Chocolate Company decreased selling prices and increased bar weights on selected items in early 1976. In December 1976, the weights and prices of its standard bars were increased. Cocoa bean market prices escalated in 1976 while sugar prices declined compared with 1975. Nevertheless, the costs in 1976 for cocoa beans as well as sugar were less than in 1975.

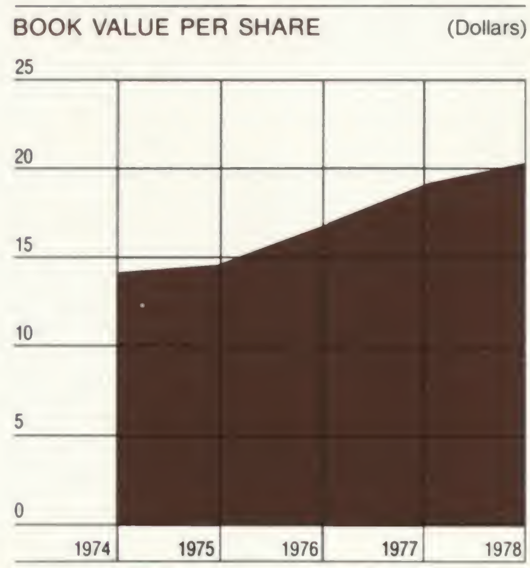
Sales dollars of chocolate and confectionery products increased substantially, reflecting higher average selling prices in 1975 compared with 1974. There was also an increase in volume of consumer units sold in 1975 compared with 1974. However, the actual poundage sold in 1975 declined as a result of lower average bar weights of many of the chocolate and confectionery items. The Company experienced unprecedented escalation in virtually all raw material costs throughout 1974 and 1975. The most significant increases were incurred in sugar and cocoa beans for chocolate and confectionery products. Although market prices of cocoa beans and sugar receded in 1975 compared with the highs of 1974, the Company's average annual costs of these commodities were higher in 1975 than in 1974. In the case of Other Food Products and Services, a significant cost increase was incurred for coffee, while the cost of flour used in pasta products declined in 1975 compared with 1974.

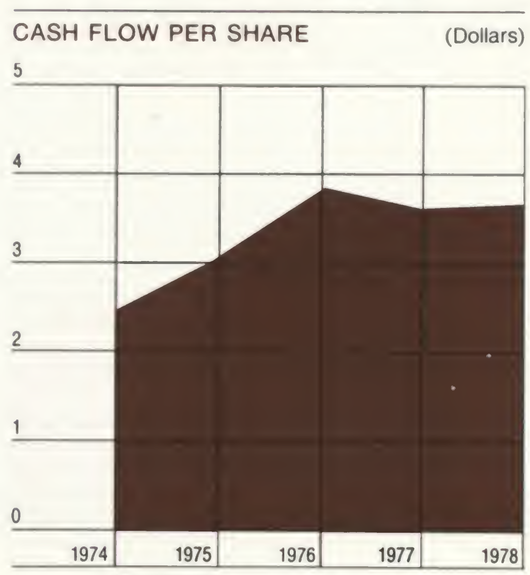
The operations of one of the Company's subsidiaries, Portion Control Industries, Inc., were discontinued in 1975. Losses from this operation were $1.4 million in 1975 and $2.3 million in 1974. In addition, the loss on disposal of this business was $4.9 million.

In 1974, a transition was made in standard bar prices so that these bars, which had sold in most retail outlets for 10¢ since 1970, sold for 15¢.

For many years, a substantial portion of the Company's major raw materials, goods in process and finished goods have been stated at cost under the LIFO method. In 1974, the Company extended LIFO inventory accounting to sugar and certain packaging materials for its chocolate and confectionery products in order to more realistically match current costs against revenue and reduce the effect of inflation on earnings. The effect of the change was to increase cost of sales by $12.4 million and decrease net income by $6.0 million or $.44 per share in 1974.







Capital Additions

Capital additions in 1978 amounted to $37.4 million. Depreciation expense for the year was $8.9 million. The Company has spent $107.3 million during the past five years.

Dividends

The Company completed its 49th year of uninterrupted dividends with the payment on December 15, 1978 of its 196th consecutive quarterly dividend on the common stock. Cash dividends paid on the Company's common stock were $16.8 million in 1978 and $14.8 million in 1977. Dividends paid per share on the Company's common stock were $1.225 in 1978.

In October 1978, the quarterly dividend was increased by the Board of Directors from $.30 to $.325. This represents the fourth consecutive year of dividend increases for the stockholders.

Investor Information

Stock Market Data

Hershey Foods Corporation had 18,735 stockholders at year-end 1978, with a total of 13,745,269 common shares outstanding. There is no other class of stock outstanding.

Hershey Foods Corporation common stock is listed and traded principally on the New York Stock Exchange under the symbol HSY. Approximately 1,300,000 shares of the Company's common stock were traded during each of the past two years, or approximately 19% of the listed shares available. The closing price of the common stock on the New York Stock Exchange on December 29, 1978 was $20.625.

The Company's common stock price range and dividends per share by quarter for the last two years appear on page 1.

Automatic Dividend Reinvestment Service

Hershey Foods Corporation stockholders may take advantage of an automatic dividend reinvestment service offered through Manufacturers Hanover Trust Company. Quarterly common stock dividends are automatically reinvested in Hershey common stock, and optional cash investments may be made for the purchase of additional shares. A brochure describing this service is available from the Company's Investor Relations Department in Hershey and from the Dividend Reinvestment Department of Manufacturers Hanover Trust Company, P.O. Box 24850, Church Street Station, New York, N.Y. 10242.

Investor Services

Hershey Foods Corporation maintains an Investor Relations Department in Hershey. Requests for interim and annual reports, or for more information about the Company, should be directed to the Investor Relations Department, 19 East Chocolate Avenue, Hershey, Pa. 17033.

Investor Relations Activities

During 1978, the Company's investor relations program continued to emphasize informational meetings with representatives from both retail and institutional investment firms as well as commercial and investment bankers. Also, on October 25, key members of the Company's senior management appeared for the first time before the New York Society of Security Analysts, one of the oldest and largest groups of analysts and investment managers in the country.

In addition to the New York Society presentation, other 1978 meetings were held in Chicago on July 20, in Milwaukee on July 21, in Philadelphia on August 30, in Pittsburgh on August 31, in San Francisco on November 7, and in Los Angeles on November 9. These meetings involved smaller groups, generally 20 to 30, and were more informal than the New York Society presentation. However, the program was much the same, including prepared comments by several members of Hershey management, followed by a question and answer session.

The investor relations program in 1979 will continue to stress these meetings as a major opportunity to communicate effectively with the investment community. The Company feels that such face-to-face contact is a valuable way to generate awareness of its accomplishments and plans for growth and development.

Consolidated Statements of Income and Retained Earnings

(in thousands of dollars except per share figures)

	For the Years Ended December 31	
	1978	1977
Net Sales	$767,880	$671,227
Costs and Expenses:		
Cost of goods sold (Note 1)	519,395	453,960
Selling, administrative and general	127,494	109,585
Shipping	32,918	28,816
Depreciation	8,850	7,995
Interest income—net	(2,683)	(509)
Total costs and expenses	685,974	599,847
Income from continuing operations before taxes	81,906	71,380
Provision for Federal and state income taxes (Note 3)	40,450	35,349
Income from Continuing Operations	41,456	36,031
Gain on sale of discontinued operation (less income taxes of $2,985) (Note 2)	—	5,300
Net Income	41,456	41,331
Retained Earnings at January 1	243,855	217,775
Deduct:		
Cash dividends	16,836	14,848
Cash dividends of pooled company prior to acquisition	—	403
Retained Earnings at December 31	$268,475	$243,855
Income per Common Share (Note 1):		
Continuing operations	$ 3.02	$ 2.62
Gain on sale of discontinued operation	—	.39
Net income	$ 3.02	$ 3.01
Cash dividends per common share	$ 1.225	$ 1.14

The accompanying notes are an integral part of these statements.

Consolidated Balance Sheets

(in thousands of dollars)

Assets

	December 31 1978	December 31 1977
Current Assets:		
Cash	$ 7,622	$ 7,980
Commercial paper and certificates of deposit	104,134	109,258
Accounts receivable—trade (less allowances for doubtful accounts of $1,322 and $1,327)	31,787	35,756
Inventories (Note 1):		
Raw materials	28,071	28,136
Goods in process	6,154	6,806
Finished goods	31,386	27,008
	65,611	61,950
Other current assets	7,505	6,258
Total current assets	216,659	221,202
Property and Equipment, at cost:		
Land	4,226	2,773
Buildings	76,190	67,904
Equipment	184,845	160,657
	265,261	231,334
Less-accumulated depreciation	94,481	88,164
	170,780	143,170
Goodwill	18,056	17,777
Other Assets:		
Investments	10,295	8,095
Other assets and deferred charges	6,214	5,909
	16,509	14,004
	$422,004	$396,153

Liabilities and Stockholders' Equity

	December 31 1978	December 31 1977
Current Liabilities:		
Accounts payable	$ 43,696	$ 55,650
Accrued liabilities	20,855	14,154
Income taxes payable	9,864	13,345
Total current liabilities	74,415	83,149
Long-Term Debt (Note 4)	35,540	29,440
Deferred Income Taxes (Notes 1 and 3)	27,660	23,896
Stockholders' Equity (Note 6)		
Common stock, without par value (stated value $1 per share)— authorized 20,000,000 shares; outstanding 13,745,269 and 13,730,288 shares	13,745	13,730
Additional paid-in capital	2,169	2,083
Retained earnings	268,475	243,855
Total stockholders' equity	284,389	259,668
	$422,004	$396,153

The accompanying notes are an integral part of these balance sheets.

Consolidated Statements of Changes in Financial Position

(in thousands of dollars)

	For the Years Ended December 31	
	1978	1977
Financial Resources Provided		
Continuing operations:		
Net Income	$41,456	$36,031
Depreciation	8,850	7,995
Deferred income taxes	3,764	4,824
Resources provided from continuing operations	54,070	48,850
Discontinued operation:		
Gain on sale	—	5,300
Deferred income taxes	—	(2,522)
Assets sold or held for disposal	—	9,239
Resources provided from discontinued operation	—	12,017
Increase in long-term debt	7,000	—
Other	482	2,906
Total resources provided	61,552	63,773
Financial Resources Applied		
Capital expenditures	37,425	27,535
Cash dividends	16,836	15,251
Increase in investments	2,200	5,498
Reduction in long-term debt	900	—
Total resources applied	57,361	48,284
Increase in Working Capital	$ 4,191	$15,489
Increase (Decrease) in Working Capital		
Cash	$ (358)	$ 3,152
Commercial paper and certificates of deposit	(5,124)	56,612
Receivables	(3,969)	(3,804)
Inventories	3,661	(4,354)
Other current assets	1,247	(276)
Accounts payable	11,954	(36,670)
Accrued liabilities	(6,701)	423
Income taxes payable	3,481	406
Increase in Working Capital	$ 4,191	$15,489

The accompanying notes are an integral part of these statements.

Summary of Significant Accounting Policies 1

The significant accounting policies followed by the Company, as summarized below, are in conformity with generally accepted accounting principles.

Principles of Consolidation
The accompanying consolidated financial statements include the accounts of the Company and its subsidiaries after elimination of intercompany accounts and transactions. The accounts and transactions of the Company's Canadian operations and foreign affiliates are translated in accordance with Financial Accounting Standards Board Statement No. 8. Charges and credits to income as a result of foreign currency translation were not material.

Inventories
Substantially all of the Hershey Chocolate Company and Y & S Candies Inc. inventories are valued under the "last-in, first-out" (LIFO) method. Such LIFO inventories amounted to approximately $42,597,000 in 1978 and $41,296,000 in 1977. Current cost, which approximates FIFO cost, exceeded LIFO cost by approximately $99,600,000 at December 31, 1978 and 1977. The remaining inventories are stated at the lower of cost or market under the "first-in, first-out" or "average cost" methods.

During 1977, the Company reduced inventory quantities, primarily cocoa beans. This reduction resulted in a liquidation of LIFO inventory quantities carried at lower costs prevailing in prior years as compared with the cost of 1977 purchases, the effect of which decreased cost of goods sold by approximately $8,500,000 and increased net income by approximately $4,000,000 or $.29 per share.

Depreciation
The Company and its subsidiaries follow the policy of providing for depreciation of buildings and improvements over estimated lives ranging from 20 to 50 years and of machinery and equipment over estimated lives ranging from 3 to 25 years. The companies have employed primarily straight-line methods in determining the annual charge for depreciation.

Major renewals and betterments are capitalized. Maintenance, repairs and minor renewals are expensed as incurred.

Goodwill
The excess cost of investments over net assets of businesses acquired is reflected as goodwill in the Consolidated Balance Sheets. It is the Company's policy to carry goodwill arising prior to November 1, 1970, at cost until such time as there may be evidence of diminution in value or the term of existence of such value becomes limited. Goodwill arising after October 31, 1970, is being amortized over a period not exceeding 40 years.

Investments
Investments include the cost of less than majority owned companies and the applicable equity in earnings since acquisition.

Development and Promotion Expenses
The costs of research and development ($2,786,000 in 1978 and $2,686,000 in 1977) and advertising and promotion are expensed in the year incurred.

Income Taxes
The provision for Federal and state income taxes is based on income recorded in the financial statements. Appropriate deferred income taxes are provided for the tax effect of timing differences resulting primarily from the use of accelerated depreciation for income tax purposes. The provision for income taxes has been reduced by allowable investment tax credits.

Retirement Plan
The Company has retirement plans covering substantially all employees. The total pension expense was $6,262,000 in 1978 and $5,832,000 in 1977. Effective in 1978, the Company changed its pension benefits and funding method and adopted the unit credit actuarial cost method of determining pension expense for the salaried employees. These changes did not have a significant effect on the calculation of pension expense. For non-salaried employees, the Company uses the entry age normal method of determining pension expense.

Unfunded prior service costs, estimated at $46,324,000, are being funded over a 30-year period. The actuarially determined value of vested benefits exceeds the market value of plan assets by approximately $20,914,000 at December 31, 1978.

Income Per Share
Income per common share has been computed based on the weighted average number of shares of common stock outstanding during the year (13,742,101 in 1978 and 13,722,147 in 1977).

2 Acquisitions and Discontinued Operations

In April 1978, the Company acquired the net assets of Procino-Rossi Corporation, a regional pasta manufacturer. This acquisition has been accounted for as a purchase and accordingly the results of its operations have been included from the date of acquisition. These results have an insignificant effect on the consolidated results of operations.

In late 1978, the Company decided to dispose of the equipment division of Cory Food Services, Inc., a manufacturer of brewing equipment primarily for use by Cory Coffee Service customers. This operation has incurred operating losses for the last several years. The provision for loss on the disposition of approximately $2,000,000 has been included in selling, administrative and general expenses in the accompanying Consolidated Statements of Income.

In November 1977, the Company acquired Y & S Candies Inc., a manufacturer of licorice-type candies, for 701,982 shares of the Company's common stock. The acquisition was accounted for as a pooling of interests. Also, in 1977, the Company acquired a 20% interest in the voting stock of AB Marabou of Sundbyberg, Sweden for $3,824,000.

In 1977, the Company sold the real estate and operating equipment of its almond ranch subsidiary, resulting in an after-tax gain of $5,300,000 or $.39 per share.

3 Income Taxes

The provision for income taxes from continuing operations exceeds taxes currently payable by $3,764,000 in 1978 and $2,303,000 in 1977, primarily because of the use of accelerated depreciation methods for income tax purposes.

The following table reconciles the provision for Federal and state income taxes on continuing operations with the amount computed by applying the Federal statutory rate.

	1978		1977	
	Amount	%	Amount	%
	(in thousands of dollars)			
Taxes computed at statutory rate	$39,315	48.0	$34,262	48.0
Increase (reductions) resulting from:				
State income taxes, net of Federal income tax benefit	3,354	4.1	3,053	4.3
Investment tax credit	(2,008)	(2.4)	(2,200)	(3.1)
Other, net	(211)	(.3)	234	.3
Provision for income taxes	$40,450	49.4	$35,349	49.5

4 Current and Long-Term Debt

Long-term debt at December 31, 1978 and 1977 consisted of the following:

	1978	1977
	(in thousands of dollars)	
7¼% Sinking Fund Debentures due 1997 with annual payments of $1,500,000	$28,500	$30,000
Less-Debentures repurchased	(3,960)	(4,560)
6⅞% Industrial Revenue Bonds due 2000 through 2005	4,000	4,000
8⅞% Promissory Notes due 1980	7,000	—
	$35,540	$29,440

On July 17, 1978, the Company, through a private placement, issued $7,000,000 of 8⅞% Promissory Notes with a maturity date of May 15, 1980. The proceeds from these notes are being used to finance construction of its research and technical center.

During 1978, the Company purchased $900,000 of its 7¼% Sinking Fund Debentures and utilized $1,500,000 of previously purchased Debentures to meet its first annual sinking fund requirement. The Company intends to use the $3,960,000 of repurchased Debentures at December 31, 1978 to meet future sinking fund requirements.

Industrial Revenue Bonds in the amount of $4,000,000 were issued on April 1, 1975, by the Dauphin County Industrial Development Authority to provide financing for certain pollution control and environmental expenditures by the Company. The Company is solely responsible for payment of principal and interest.

As a result of seasonal working capital requirements, the Company maintains lines of credit of $60,000,000 with several domestic banks. There were no borrowings in 1978 or 1977 under these lines of credit. While there are no compensating balance agreements which legally restrict funds, the Company has been expected to and has generally maintained average compensating balances of 15% to 20% of borrowings or generally not less than 5% of commitments.

In December 1978, in connection with the acquisition of Friendly Ice Cream Corporation (see Note 12), the Company obtained a revolving credit and term loan agreement with four banks which provided for borrowings of up to $200,000,000. This loan commitment was reduced to $100,000,000 effective on January 22, 1979. The agreement requires the Company to pay a commitment fee of ½% per annum on the average daily unused portion of the loan commitment. Further, the Company pays interest on the aggregate, unpaid principal amount of all borrowings at a rate equal to the higher of the base rate of Citibank, N.A., or the 90 day dealer-placed commercial paper rate plus ½ of 1%. Assuming a base rate of 11.5%, the effective annual interest rate on the borrowings under the agreement, after giving effect to compensating balances, is 12.8%. The agreement also contains certain restrictive covenants on working capital, tangible net worth and total amount of debt. There were no borrowings under this agreement in 1978. Any borrowings outstanding as of December 31, 1980, will be converted into a six-year term loan.

Lease Commitments 5

The Company has principally operating lease agreements for office space, autos and equipment, the aggregate annual cost of which is less than 1% of net sales.

Stock Option Plan 6

On November 30, 1977, a Hershey Foods Corporation Stock Option Plan was adopted as a substitute for the Y & S Candies Inc. 1970 Stock Option Plan pursuant to the Agreement and Plan of Reorganization between Y & S and the Company dated October 12, 1977.

At December 31, 1978, 15,905 options were outstanding at prices ranging from $3.06 to $6.85. No shares were available for future grant under the Plan. The excess of proceeds over the stated value of the stock issued under the Plan is credited to additional paid-in capital; no charge is made to income with respect to these options. During 1978, 14,970 shares were exercised under the Plan at prices ranging from $6.56 to $6.85. The Plan terminates on September 14, 1980, the last day outstanding options are exercisable.

Savings and Stock Investment Plan 7

On July 1, 1978, the Company adopted a Savings and Stock Investment Plan for its salaried employees. Under the Plan, participating employees authorize payroll deductions of up to 4 percent of their earnings assigned to various investment options under the Plan. The Company contributes an amount equal to 50 percent of the participating employee payroll deduction. The Company contributions, which amounted to $253,000 in 1978, are used by the Plan's independent trustee to purchase the Company's common stock at prevailing market prices for distribution to participating employees. The common stock vests with the employee four years after the date of such Company contributions.

Management Incentive Plan 8

The Company has a management incentive plan providing incentive compensation to eligible employees of the Company and its subsidiaries who have substantial managerial or similar responsibilities. The Plan currently includes both annual and long-term incentive compensation programs. The amount charged to expense in 1978, including the first-year accrual under the long-term incentive program, was $1,300,000. The amount charged to expense in 1977 was $901,000.

9 Industry Segments

Industry segment information is shown on page 38 of this report.

10 Summary of Quarterly Data (Unaudited)

(in thousands of dollars except per share figures)

Year 1978	First	Second	Third	Fourth	Year
Net sales	$190,883	$151,814	$201,374	$223,809	$767,880
Gross margin	60,282	48,151	65,055	74,997	248,485
Net income	$ 10,317	$ 6,170	$ 11,627	$ 13,342	$ 41,456
Net income per common share	$ .75	$ .45	$ .85	$ .97	$ 3.02

Year 1977	First	Second	Third	Fourth	Year
Net sales	$173,070	$124,117	$177,543	$196,497	$671,227
Gross margin	54,625	40,505	52,555	69,581	217,266
Income from continuing operations	8,778	4,820	8,221	14,212	36,031
Gain on sale of discontinued operation	—	5,300	—	—	5,300
Net income	$ 8,778	$ 10,120	$ 8,221	$ 14,212	$ 41,331
Income per common share:					
Continuing operations	$ .64	$ .35	$ .60	$ 1.03	$ 2.62
Gain on sale of discontinued operation	—	.39	—	—	.39
Net income	$ .64	$ .74	$ .60	$ 1.03	$ 3.01

11 Impact of Inflation (Unaudited)

The Company's products and services have been subject in varying degrees to the inflation affecting the general economy and the goods and services purchased by the Company.

Since the major portion of inventories are costed at LIFO (last-in, first-out) the rapid escalation in product costs has been substantially reflected currently in cost of sales. The same situation does not exist with respect to plant and equipment and related depreciation charges. The cumulative impact of inflation over a number of years would result in replacement cost of existing plant and equipment and related depreciation being higher than actual historical cost. Reference is made to the Annual Report Form 10-K (copy available on request) for additional information with respect to the estimated replacement cost of inventories and plant and equipment at December 31, 1978 and 1977, and the related estimated effect of such costs on cost of sales and depreciation expense for the years then ended.

12 Subsequent Events

Effective January 3, 1979, the Company acquired the outstanding shares of common stock of Skinner Macaroni Company, in exchange for 398,680 shares of the Company's common stock. Skinner manufactures and distributes pasta products in approximately 20 states. This acquisition, which is not material to the consolidated financial statements, will be accounted for as a pooling of interests in 1979.

On January 18, 1979, the Company entered into a joint venture agreement in Brazil with S.A. Industrias Reunidas F. Matarazzo to manufacture, market and distribute pasta, biscuits and margarine and also distribute certain products manufactured by the food division of Matarazzo. The Company's investment of approximately $7,500,000 represents a 40% equity interest. Matarazzo is a long-established, major diversified industrial firm in Brazil.

As a result of a cash tender offer which expired January 19, 1979, the Company acquired substantially all of the outstanding common stock of Friendly Ice Cream Corporation. The Company expects that Friendly will become a wholly-owned subsidiary through a merger in late March 1979 and that the total cost will approximate $164,000,000. The Company borrowed $100,000,000 under its revolving credit and term loan agreement as part of the financing for this acquisition (see Note 4). The Company currently expects to refinance $75,000,000 of such borrowings through the issue and sale of long-term debt securities and the balance through short-term borrowings. Friendly owns and operates over 600 restaurants located in 16 states throughout the northeast and midwest. The acquisition will be accounted for as a purchase and accordingly Friendly's results of operations will be included with the Company's consolidated results of operations for periods subsequent to the date of acquisition. Consequently the Company's consolidated financial statements for 1979 will include the results of operations of Friendly for eleven months.

The following table summarizes, on an unaudited pro forma basis, the combined results of operations for 1978 and 1977 (including estimated amortization of goodwill, depreciation adjustments and interest expense on funds expended for this acquisition) as though Friendly had been acquired on January 1, 1977 (in thousands of dollars except per share figures):

	1978	1977
Net sales	$981,251	$860,221
Income from continuing operations	$ 44,437	$ 38,413
Gain on sale of discontinued operation	—	5,300
Net income	$ 44,437	$ 43,713
Income per common share:		
Continuing operations	$ 3.23	$ 2.80
Gain on sale of discontinued operation	—	.39
Net income	$ 3.23	$ 3.19

The pro forma amounts are based on the Company's audited results of operations for the twelve months ended December 31, 1978 and 1977, and Friendly's unaudited results of operations for the twelve months ended October 27, 1978, and October 28, 1977, respectively.

Auditors' Report

To the Stockholders and Board of Directors
of Hershey Foods Corporation:

We have examined the consolidated balance sheets of Hershey Foods Corporation (a Delaware corporation) and subsidiaries as of December 31, 1978 and 1977, and the related consolidated statements of income and retained earnings and changes in financial position for the years then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the accompanying consolidated financial statements present fairly the financial position of Hershey Foods Corporation and subsidiaries as of December 31, 1978 and 1977, and the results of their operations and changes in their financial position for the years then ended, in conformity with generally accepted accounting principles consistently applied during the periods.

Arthur Andersen & Co.

New York, N.Y.
February 12, 1979.

Industry Segment Information

The Company operates principally in two industry segments: Chocolate and Confectionery and Other Food Products and Services. Operations in the Chocolate and Confectionery segment involve production and sale of a full line of mass-distributed chocolate and confectionery products. The principal product groups sold are bar candy, bagged candy, chocolate drink mixes, baking ingredients, and dessert toppings. The Other Food Products and Services operations are involved in the operation of a coffee service plan for businesses and institutions, the manufacture of certain equipment (to be disposed of in 1979), and the manufacture and sale of pasta products.

Sales by segment as reported in the Company's Consolidated Statements of Income and Retained Earnings do not include intersegment sales, since such sales are immaterial and have been eliminated in consolidation.

Operating profit is total revenue less operating expenses. In computing operating profit, none of the following items have been included: general corporate expenses, interest income-net, or income taxes.

Identifiable assets are those assets that are used in the Company's operations in each industry. Corporate assets are principally cash, marketable securities, and corporate property and equipment.

No customer, government or otherwise, constitutes 10% or more of sales. Foreign sales and assets constitute less than 10% of total sales and assets.

The following table sets forth information about the Company's operations by industry segment for the five years ended December 31, 1978:

	For the Years Ended December 31				
	1978	1977	1976 (unaudited)	1975 (unaudited)	1974 (unaudited)
	(in thousands of dollars)				
Net sales:					
Chocolate and Confectionery	$678,652	$586,882	$526,822	$503,263	$438,313
Other Food Products and Services	89,228	84,345	75,138	72,902	72,770
Total net sales	$767,880	$671,227	$601,960	$576,165	$511,083
Operating profit:					
Chocolate and Confectionery	$ 79,143	$ 69,834	$ 86,898	$ 83,551	$ 50,269
Other Food Products and Services	5,061	4,528	5,005	3,549	2,664
Total operating profit	84,204	74,362	91,903	87,100	52,933
General corporate expenses	(4,981)	(3,491)	(2,299)	(1,642)	(727)
Interest income (expense)—net	2,683	509	(357)	(1,264)	(2,279)
Income from continuing operations before taxes	$ 81,906	$ 71,380	$ 89,247	$ 84,194	$ 49,927
Identifiable assets:					
Chocolate and Confectionery	$241,070	$221,928	$222,541	$217,772	$208,504
Other Food Products and Services	50,450	47,023	44,325	44,152	45,142
Corporate	130,484	127,202	65,004	44,627	34,450
Total identifiable assets	$422,004	$396,153	$331,870	$306,551	$288,096
Depreciation:					
Chocolate and Confectionery	$ 6,574	$ 5,702	$ 5,439	$ 5,566	$ 5,538
Other Food Products and Services	1,720	1,789	1,755	1,760	2,137
Corporate	556	504	345	215	253
Total depreciation	$ 8,850	$ 7,995	$ 7,539	$ 7,541	$ 7,928
Capital expenditures:					
Chocolate and Confectionery	$ 23,923	$ 22,381	$ 17,227	$ 8,489	$ 7,246
Other Food Products and Services	4,420	3,014	1,754	1,995	2,884
Corporate	9,082	2,140	1,741	58	954
Total capital expenditures	$ 37,425	$ 27,535	$ 20,722	$ 10,542	$ 11,084

Five-Year Financial Summary

Hershey Foods Corporation and Subsidiaries
(All dollar and share figures in thousands—except market price and per share statistics)

	1978	1977	1976	1975	1974
Summary of Earnings					
Continuing Operations					
Net Sales	$ 767,880	671,227	601,960	576,165	511,083
Cost of Goods Sold	$ 519,395	453,960	383,664	381,115	373,277
Operating Expenses	$ 169,262	146,396	128,692	109,592	85,600
Interest Expense	$ 2,620	2,422	2,240	3,126	3,710
Interest Income	$ 5,303	2,931	1,883	1,862	1,431
Income Taxes	$ 40,450	35,349	45,562	43,292	25,718
Income from Continuing Operations	$ 41,456	36,031	43,685	40,902	24,209
Income (Loss) from Discontinued Operations	$ —	—	1,112	(1,457)	(1,608)
Gain (Loss) Related to Disposal of Discontinued Operations	$ —	5,300	—	(4,898)	—
Net Income	$ 41,456	41,331	44,797	34,547	22,601
Income Per Share of Common Stock					
Continuing Operations	$ 3.02	2.62	3.18	2.99	1.77
Discontinued Operations	$ —	—	.08	(.11)	(.12)
Gain (Loss) Related to Disposal	$ —	.39	—	(.36)	—
Net Income	$ 3.02	3.01	3.26	2.52	1.65
Dividends per—Common Share	$ 1.225	1.14	1.03	.85	.80
Preferred Share	$ —	—	—	.60	.60
Average Number of Common Shares and Equivalents Outstanding During the Year	13,742	13,722	13,720	13,698	13,685
Per Cent of Income from Continuing Operations to Sales	5.4%	5.4%	7.3%	7.1%	4.7%
Financial Statistics					
Capital Expenditures	$ 37,425	27,535	20,722	10,542	11,084
Depreciation*	$ 8,850	7,995	7,539	7,541	7,928
Advertising*	$ 21,847	17,637	13,330	9,499	1,814
Current Assets	$ 216,659	221,202	169,872	157,579	129,226
Current Liabilities	$ 74,415	83,149	47,309	53,808	59,156
Working Capital	$ 142,244	138,053	122,563	103,771	70,070
Current Ratio	2.9:1	2.7:1	3.6:1	2.9:1	2.2:1
Long-Term Debt	$ 35,540	29,440	29,440	29,856	31,730
Debt-to-Equity Per Cent	13%	11%	13%	15%	18%
Stockholders' Equity	$ 284,389	259,668	233,529	202,466	178,238
Stockholders' Data					
Outstanding Common Shares at Year-End	13,745	13,730	13,720	13,720	12,485
Market Price of Common Stock—					
At Year-End	$ 20⅝	19⅞	22⅜	18⅝	9¾
Range During Year	$18½–23½	16⅝–22⅜	18½–27½	10⅛–20⅞	8½–15
Number of Common Stockholders	18,735	19,694	20,421	19,686	19,769
Employees' Data					
Payrolls	$ 112,135	99,322	88,848	78,973	77,484
Number of Employees—Year-End	8,100	7,660	7,670	7,580	7,740

*Restated to reflect continuing operations only.

John S. Harkins
Vice President
Finance and Commodities

Dr. Ogden C. Johnson
Vice President
Science and Technology

Richard M. Marcks
Vice President
International



William P. Noyes
Vice President
Human Resources

William F. Suhring
Vice President
Corporate Development

William Lehr Jr.
Secretary



Michael F. Pasquale
Controller

Kenneth L. Wolfe
Treasurer

Earl J. Spangler
President
Hershey Chocolate Company



Robert J. Gaudrault
Chairman and Chief Executive Officer
Friendly Ice Cream Corporation

Joseph P. Viviano
President
San Giorgio Macaroni, Inc.

Lloyd E. Skinner
Chairman and Chief Executive Officer
Skinner Macaroni Company



Charles A. Smylie
President
Y & S Candies Inc.

David B. Conn
President
Hershey Chocolate of Canada

George E. Wilber, Jr.
President
Cory Food Services, Inc.



Board of Directors

Harold S. Mohler, *Chairman*
William E. Dearden, *Vice Chairman*
Richard T. Baker
Consultant and Former Managing Partner, Ernst & Ernst
John C. Jamison
Investment Banker, Partner, Goldman, Sachs & Co.
Francine I. Neff
Vice President, Rio Grande Valley Bank, Albuquerque, N.M.
Samuel A. Schreckengaust, Jr.
Vice President and General Counsel
Philip A. Singleton
President, Singleton Associates International
Louis C. Smith
Vice President
John C. Suerth
Chairman of the Executive Committee, Director, Gerber Products Company
Richard A. Zimmerman
President and Chief Operating Officer

Executive Committee

Harold S. Mohler, *Chairman*
William E. Dearden
Samuel A. Schreckengaust, Jr.
Richard A. Zimmerman

Audit Committee

Philip A. Singleton, *Chairman*
Richard T. Baker
John C. Jamison
John C. Suerth

Compensation Committee

John C. Jamison, *Chairman*
Richard T. Baker
Philip A. Singleton
John C. Suerth

Employee Benefits Committee

Samuel A. Schreckengaust, Jr., *Chairman*
John C. Jamison
Francine I. Neff
Philip A. Singleton
John C. Suerth

Corporate Officers

Harold S. Mohler, *Chairman of the Board*
William E. Dearden, *Vice Chairman of the Board and Chief Executive Officer*
Richard A. Zimmerman, *President and Chief Operating Officer*
John S. Harkins, *Vice President, Finance and Commodities*
Dr. Ogden C. Johnson, *Vice President, Science and Technology*
Richard M. Marcks, *Vice President, International*
William P. Noyes, *Vice President, Human Resources*
Samuel A. Schreckengaust, Jr., *Vice President and General Counsel*
Louis C. Smith, *Vice President*
William F. Suhring, *Vice President, Corporate Development*
William Lehr Jr., *Secretary*
Kenneth L. Wolfe, *Treasurer*
Michael F. Pasquale, *Controller*

Annual Meeting

The Annual Meeting will be held at 2 p.m. on Monday, April 30, 1979, at the Hershey Motor Lodge and Convention Center, Route 322 and University Drive, in Hershey.

A formal notice of this meeting, together with a proxy statement, will be mailed to stockholders on or about March 23, 1979.

Stockholders who are unable to attend the meeting are urged to sign and return their proxies promptly so the stock of the Company will be represented as fully as possible at the meeting.

Form 10-K

The Annual Report to the Securities and Exchange Commission on Form 10-K is available upon written request to the Secretary of the Corporation, 100 Mansion Road East, Hershey, Pa. 17033.

Principal Securities Market

The common stock is listed on the New York Stock Exchange.

Executive Offices

100 Mansion Road East
Hershey, Pa. 17033

Transfer Agent and Registrar

Manufacturers Hanover Trust Company
4 New York Plaza
New York, N.Y. 10015

Auditors

Arthur Andersen & Co.
New York

Hershey Foods Corporation
Hershey, Pa. 17033, U.S.A.

HERSHEY
PENNSYLVANIA

BULK RATE
U.S. POSTAGE
PAID
PERMIT No. 33